Bulgaria Launches Corporate Governance Code

On the brink of Bulgaria's accession to the European Union, a task force comprised of private and public experts was set up to develop a national Corporate Governance Code. Such best practice codes (not to be confused with a civil law corpus of laws) exist already in many countries; their adoption is recommended by the EU’s Transparency Directive.

Codes are effective tools for helping companies improve their governance practices; provide clearer guidance for financial and non-financial disclosure; foster better engagement of minority shareholders; and, clarify the respective roles of managers and directors.

“A Corporate Governance Code was much needed for Bulgaria to support the business community’s efforts to compete on the EU and international markets. It would give companies that wanted to apply better governance practices, the opportunity to distinguish themselves,” said Bistra Boeva, of the University for National and World Economic Studies and co-chair of the task force. “Doing so would inspire investor and lender confidence.”

The Forum had previously published a Toolkit (Corporate Governance Reform Toolkit 2), which provides extensive practical experiences from developed and developing countries on how to develop and implement corporate governance codes.

"Building on the global expertise we compiled in this toolkit, we provided the Bulgarian team with best practices and technical advice,” said Marie-Laurence Guy, a senior projects officer with the Forum. “But we didn’t draft the code for them. The code might have been structured differently and included higher standards if we would have hired an international consultant to draft it, but it would have resulted in a window dressing exercise. It’s their code, not ours; local ownership makes for better enforcement.”

“The Forum’s expertise and experiences provided Bulgaria with practical, relevant, insightful counsel.”

Prof. Bistra Boeva
Co-Chair, Bulgaria Corporate Governance Code Task Force

A corporate governance code must reflect the level of best practices that can be handled and implemented by a country’s companies, with a certain level of measured aspirations to higher standards. The code was launched on October 9, 2007 and quickly adopted by the Bulgarian Stock Exchange. The listing rules now...
require companies to comply with the code or explain and disclose why they did not or could not comply with certain provisions. Non-listed companies are encouraged to follow the code’s core recommendations in accordance with their abilities and ambitions.

“The Global Corporate Governance Forum welcomes the development of Bulgaria’s new code, which sets higher standards than those in the country’s current laws and regulations,” said Philip Armstrong, the Forum’s head. “Countries like Bulgaria must set corporate governance standards that go beyond mere legal requirements to encourage internationally acceptable rules of behavior and conduct for boards, directors, and companies. This is an essential precondition for attracting domestic and international investors’ capital.”

Ensuring Effective Support

Why is a code needed?

What are the issues to be dealt with?

What can the code achieve?

What companies should be targeted?

How will the code be implemented and monitored?

Momentum counters the inevitable ups and downs of a project of this scale and nature. The code development process often takes more time than expected—at least a year. Even if forewarned, there is always the danger that task force members lose interest or get distracted by new priorities. Ensuring that all the key stakeholders stay involved and actively contribute to the process—this is the biggest challenge from the technical advisory perspective.

In Bulgaria, task force meetings were initially held in English and allowed for the participation of international experts from the Forum’s Private Sector Advisory Group (PSAG). Yet, to get the drafting phase started, the team switched to Bulgarian to make the process more effective.

“Once the first full draft is completed, it is important to include public consultation,” said Guy. “It offers the possibility for target users to provide feedback and to feel engaged in the process.” In Bulgaria, this process turned out to be an excellent awareness-raising tool for corporate governance in general, generating extensive news coverage, online discussions, and conferences.

How a code is expected to be implemented needs to be discussed early in the process. The Bulgarian team chose to recommend the “comply or explain” principle and had the exchange agree to make the code part of its listing rules.
prior to the code’s launch. This enforcement approach makes it mandatory for listed companies to disclose whether they are in compliance with the code’s provisions, but offers the flexibility of providing an explanation when compliance has not been achieved.

“You can’t wait for a code to be launched to decide how it will be enforced and monitored,” Guy said. “If you don’t have a clear plan on how to take things from there, goodwill and task force members will disperse, and little will happen.” The process by which a code will be enforced, monitored, and updated should be presented in the code’s introduction.

At the code’s launch, Gian Piero Cigna, counsel, the European Bank for Reconstruction and Development, rightly stressed that, “The launch of the Bulgarian code is an important first step but not a final goal. It is now important to promote compliance and monitor implementation.”

Next Steps

Best practice codes are much more flexible than laws and should be reviewed and updated regularly to address issues unforeseen during the drafting process and to remain relevant. Bulgaria’s Financial Supervision Commission (FSC) has, therefore, asked that the task force remain as a Standing Corporate Governance Commission to monitor progress and update the code’s content in 18 months so that it reflects changes in corporate practice and legislation.

PSAG member Christian Strenger has already offered to assist the commission in designing a corporate governance scorecard to help companies monitor code adherence.

The Bulgarian code is expected to inform the revision of the country’s securities law. While some code provisions may be made legally binding, the law will also see that disclosure on code compliance is mandatory—thus enhancing enforcement.

Successful cooperation with the Forum on this project has furthermore led to a formal invitation by the FSC for the World Bank to conduct a Corporate Governance Report on the Observance of Standards and Codes.

The priority is now for Bulgaria’s private sector to find an appropriate way to improve director professionalism and to institutionalize director training in accordance with the code’s recommendations.

RESULTS

- Code launched October 19, 2007
- Extensive media coverage, broad public awareness
- Code endorsed by main business, investor, industrial associations
- Stock exchange requires listed companies to comply with the code or explain reasons for non-compliance
- Securities regulator to adopt code in legal revisions and make certain provisions mandatory

FACTORS FOR SUCCESS

- A clear rationale that will build support
- Well-selected task force members to ensure the right level of expertise and support
- A widely respected chairperson
- Private sector involvement to foster ownership and deepen commitment
- Sustain momentum to survive challenges
- International expertise to share best practices, offer feedback, provide objectivity
- Pro-active consultation process to engage stakeholders and raise awareness
- Explicit implementation and monitoring strategy
CORPORATE GOVERNANCE IS ABOVE ALL CARE FOR THE OWNERSHIP

Below is an extract of an interview by Chavdar Parvanov with Bistra Boeva, one of the leaders of Bulgaria’s Corporate Governance Code Project, which appeared in the daily newspaper Dnevnik on October 23, 2007.

What is the expected impact of the launch of the Corporate Governance Code? Will corporate disclosures improve?
The code offers rules of conduct that go beyond established legal regulations without violating them and provides an opportunity for businesses to adopt better corporate governance practices. The code not only says what must be done but also explains how to do it. It provides practical instructions and guidance for applying the principles of corporate governance. The effect will be clear – improved productivity due to the application of good corporate governance in Bulgaria.

Will the Code be mandatory for the publicly traded companies in Bulgaria and will it apply to them only?
The Code is not addressed to publicly traded companies only. Undoubtedly, though, it is of great importance to them given the fact that, by law, they must comply with rules of good corporate governance. The idea, however, is that the Code should be used by all who believe in the value of good corporate governance standards – small and medium-size businesses, as well as enterprises with state and municipal ownership.

State and municipally owned companies are leaders in the area of non-transparency and non-disclosure of information. What stands in the way of having the standards and rules apply to them, too?
This problem exists not only in Bulgaria. Some countries, such as the Scandinavian ones, have also sought to apply good corporate governance standards in companies with state and municipal ownership. At the initiative of its member-countries, the Organisation for Economic Co-operation and Development has passed rules for the application of corporate governance standards in state-owned enterprises and those owned by municipal governments. These rules serve as a foundation for the proposal made by experts and legislators years ago to add text to the Public Offering of Securities Act that would bind enterprises with a majority interest of the state and municipal governments to disclose information just as publicly-held companies do. It turned out, though, that this was difficult to achieve. Very few state and municipal companies complied with this requirement, and it was difficult to monitor whether they were in compliance. As a result, this regulation was revoked. I note that, under the pretext of secrecy, a number of enterprises with state ownership do not disclose information.

Can this problem be solved if state companies offer minority shares on the stock exchange?
This is one possible step. When the State is a co-owner of such an enterprise, it must comply with the corporate governance rules in light of its public status. Based on the practice existing in other countries, I think that this is not necessary if the State, in its capacity as a shareholder, takes upon itself the obligation to follow good corporate governance practices. However, we often find ourselves in the following conflict. On the one hand, the State, as a market regulator represented by the Commission for Financial Supervision, strictly monitors compliance with [the regulations of] the Public Offering of Securities Act and other legislative acts that concern corporate governance. On the other hand, the State as an owner does not always follow the good rules.